FERC's Market Competition Conference
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Panel 2: Improving Opportunities for
Long-Term Power Contracting in Organized Markets

Remarks of Pedro J. Pizarro
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Good afternoon, Chairman Kelliher and Commissioners. I am Pedro Pizarro, the Senior Vice President of Power Procurement for Southern California Edison. SCE appreciates the Commission's commitment to competitive wholesale power markets, and the opportunity to speak here today.

SCE is a major purchaser in the wholesale market. Two-thirds of the electricity we deliver to our customers comes from market sources, with around $7 billion in power and gas transactions annually, and with nearly 17% of our energy provided by renewables. We work within a Procurement Plan approved by the California Public Utilities Commission targeting State policy objectives, with energy efficiency, demand response, renewables, and distributed generation prioritized over more conventional supply resources. The CPUC oversees our activities fully and gets further support from an external Procurement Review Group and an Independent Evaluator. Since 2001, we have conducted multiple renewable and all-source power and natural gas solicitations, contracting for many thousands of MWs.

You asked us if there are barriers to long term contracts. Around 92% of our energy in 2007 will come from long-term commitments – through both ownership and contracts – with terms of 5 years or more. However, we face real concerns with further long-term contracts. I will start with the three most significant issues, which may be outside this Commission's jurisdiction; I will then cover areas where you can help.

The first issue affecting long-term contracts is retail, not wholesale. California was one of the first states in the nation to allow retail choice. We saw Direct Access levels swing quickly with changing rules, going from near zero to about 15%, back down to 1%, and back up to about 15% over a very short period of time. California suspended new Direct Access in 2001. However, State policy makers have stated their intention to reopen retail competition, under rules yet to be developed.

This puts us in a tenuous situation. Currently, SCE and other utilities are the only entities doing any significant long-term contracting. Competitive retail providers say that long-term contracts are not compatible with their business model. SCE cannot be expected to fulfill the role of the default provider, signing long-term contracts to create a reliable system for all customers, not just our own, while also being at risk of having customers depart to Energy Service Providers who have not made – and have no obligation to make – any long-term commitments, leaving our remaining customers with stranded contracts and higher rates.

Second, the financial industry views long-term power contracts as fixed financial obligations equivalent to debt. The longer the contract, the higher the debt equivalence that credit rating agencies impute on our balance sheet when assessing our credit quality. In addition, SCE's counterparties often require us to post cash or letters of credit. These items burden our balance sheet, creating higher financing costs for our customers, and reducing our capacity to finance transmission and other infrastructure investments.

Third, California is in the early stages of implementing AB32, the greenhouse gas legislation. The California Air Resources Board is currently developing rules that will impact how we procure long-term contracts. We simply do not know today what all those impacts will be.

There are, however, areas where this Commission can support long term contracts. First, we commend your willingness to tackle the impediments to Integrated Resource Planning created by the current Standards of Conduct. We need to get the right generation in the right places in our resource selection and grid planning processes. The existing SOCs severely inhibit individuals evaluating long-term bids from accessing transmission information essential to the process. The Commission's NOPR attempts to alleviate that issue. But, as discussed in SCE's comments, the Commission should return to a Functional Approach for determining access to information, and narrow the employees precluded from receiving Non-Public Transmission Information to those in shorter-term trading activities. Such an approach focuses on the individual's job description, as opposed to the organization within which she or he works.

Second, SCE is looking forward to the Commission's decision in the Market Based Rate Authority NOPR proceeding. We appreciate your efforts to codify in one place the tests for market power. In this, SCE urges the Commission to find that liquidated damages and call option contracts should not be in the calculation of an entity's capacity, and that an entity's ownership of sites for future generation development should not be considered in market power tests.

Third, California needs new generation, and this requires long-term contracts in today's market. We support the notion that competitive markets may be able to deliver new generation without long-term contracts in the future if generators and their financiers view market frameworks as stable over the long term. However, this is not happening yet, and our State needed new resources to commence development now. California adopted a transitional mechanism by which SCE can make long-term commitments for new generation needed across our entire distribution system and pass on the benefits and costs to all customers, regardless of their retail service provider. SCE launched an RFO and has already signed 3 contracts for around 1,200 MW of new generation, with more being considered. This is only a transitional solution because our balance sheet cannot handle unlimited purchases on behalf of others, and because other load serving entities are not especially fond of us purchasing on their behalf. The long-term solution is a centralized capacity market. If designed well, it can:

- support existing generation and construction of new generation, in the right locations, as needed to meet load growth and reliability, either through several-year-forward price signals or through backstop long-term contracts for new generation;

- fairly allocate the benefits and costs associated with that capacity;

- and mitigate market power in the presence of a mandated resource adequacy and capacity requirement.

We need the Commission to support the development of this capacity market.

Finally, SCE appreciates your efforts to support new transmission infrastructure, including transmission investment incentives, the Commission's backstop siting authority, and support for transmission facilities reaching locationally-constrained generation resources, such as the Tehachapi area in California. Your efforts will help utilities secure additional resources to meet customers' needs and the State's policy objectives. One more action you can take is to ensure that long term transmission rights can be established when generation and transmission infrastructure investment decisions are made, rather than waiting until the facilities are built.

Thank you again for the opportunity to speak with you today. I look forward to addressing any questions.